Introduction

This report provides an update on the City and School District of Philadelphia's (SDP) projected year-end financials, as City Council prepares to return to session in September. Over the past decade – and particularly during the last fiscal year (FY19) – continued economic expansion has led to end-of-year General Fund balances and revenues that consistently exceed projections.

As a reminder: the City of Philadelphia's fiscal year runs from July 1st to June 30th. The Q4 City Managers Reports show the City's preliminary year-end revenues, obligations, and fund balances. FY19 'actual' figures are unaudited figures, and are subject to change.

Progress since Fiscal Year 2012 (FY12)

The **City of Philadelphia has made significant financial progress since FY12,** with respect to addressing its unfunded pension liability, funding education, stabilizing the School District of Philadelphia's finances, and achieving more sound fiscal stability overall. Here are some examples of the actions the Administration and City Council have taken to better achieve fiscal stability:

- **Increased education funding by $640 million annually[1]**, further shoring up the SDP's financial status – which allowed SDP to realize a Credit Rating Upgrade to investment grade (no longer 'junk' status).
- **Deposited almost $35 million into the Budget Stabilization Fund (Rainy Day Fund) at the beginning of FY20, for the first time ever** (with planned deposits for each of the next four years, as shown in the City's FY20-24 Five-Year Plan).
- **Recently borrowed $293 million in General Obligation Bonds at historically low rates** (in 8/2019).
- **Achieved Pension Reform** by implementing stacked-hybrid plans for most new employees (capping the defined benefit at $65,000), increasing current employee contributions, continually lowering the assumed/target rate of return, increasing passively managed funds, decreasing management fees, rebalancing the Asset Allocation, and implementing a Revenue Recognition Policy.
  - **These actions contributed to the Fund becoming net cashflow positive** (more dollars contributed to the Fund than paid out to beneficiaries) – for the first time in recent history.
  - The Pension Fund also **outperformed peer cities** in a recent Stress Test study, conducted by PEW.
  - These steps **improved the risk profile and the long-term solvency** of the Fund.

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[1] FY19 Q4 projection compared to FY12 Actual Local Tax and Non-Tax Revenues.

- **Exceeded the City's internal target General Fund end-of-year balance goal of 6-8% of revenues**
    - The ity ended FY18 with a fund balance of $369 million, and
    - The City is projected to end FY19 with a fund balance exceeding $297 million.

City of Philadelphia Q4 Highlights[2]

- The City ended the fiscal year with a **projected FY19 Year-End General Fund Balance of $297.7 million.** This projected FY19 Year-End Fund Balance figure is:
    - **$16.8 million higher than the Q3 projection**. *Note, as seen in previous fiscal years, the audited actual year-end amount could be adjusted significantly from the Q4 preliminary figure.*
    - **$158.2 million higher** than projected in the Adopted Budget – which was passed by Council in June 2018.
    - **6.3% of annual General Fund revenues**, which is within the City's internal goal of 6-8%.
        - As shown in the in the second chart on the following page, the City is currently meeting its own internal goals for the General Fund Balance, but is still below the Government Finance Officers Association (GFOA) recommendation of 16-17% of annual revenues.[3]

- **Local Tax revenues** ended the fiscal year with a projected **$106.5 million positive variance above** the original estimates in the Adopted Budget.
    - *Business Income & Receipts* (BIRT) ended the fiscal year with a projected $78.1 million positive variance, above Adopted Budget estimates.
    - *Real Estate Transfer Tax* (RTT) ended the fiscal year with a projected $334.7 million, which would be $24.2 million above Adopted projections.
    - *Wage and Earnings Taxes* ended the fiscal year with a projected $22.3 million negative variance, compared to Adopted estimates, but still showed year-over-year growth. This tax ended FY19 with a projected $24 million positive variance above FY18 revenues.

- **General Fund revenues and obligations have grown considerably since FY12.** If the Q4 preliminary actuals *are not* adjusted:
    - Annual *General Fund revenues* will have increased by $1.15 billion since FY12.
        - FY12 Actual: $3.6 billion
        - FY19 Preliminary Actual: $4.7 billion
    - Annual *General Fund obligations* will have increased by $1.34 billion since FY12[4].
        - FY12 Actual: $3.5 billion
        - FY19 Preliminary Actual: $4.8 billion

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[2] The *Finance and Budget Team* plans to release an updated report in the Fall (2019), highlighting the final year-end figures in conjunction with the release of the *Annual Financial Report.*

[3] Government Finance Officers Association: *Fund Balance Guidelines for the General Fund* (2015)

[4] FY20 Obligations include a combined $311.8 million in pass-through funding and placeholders for reserves. In FY20, it is anticipated that $222.5 million will be sent to the School District through the Department of Finance line-item, $55.1 million is listed as a contingency for unanticipated cuts in federal funding (*Federal Funding Reserve)*, and a $34.2 million deposit is budgeted for the *Budget Stabilization Reserve (*a.k.a the *"Rainy Day Fund")*.
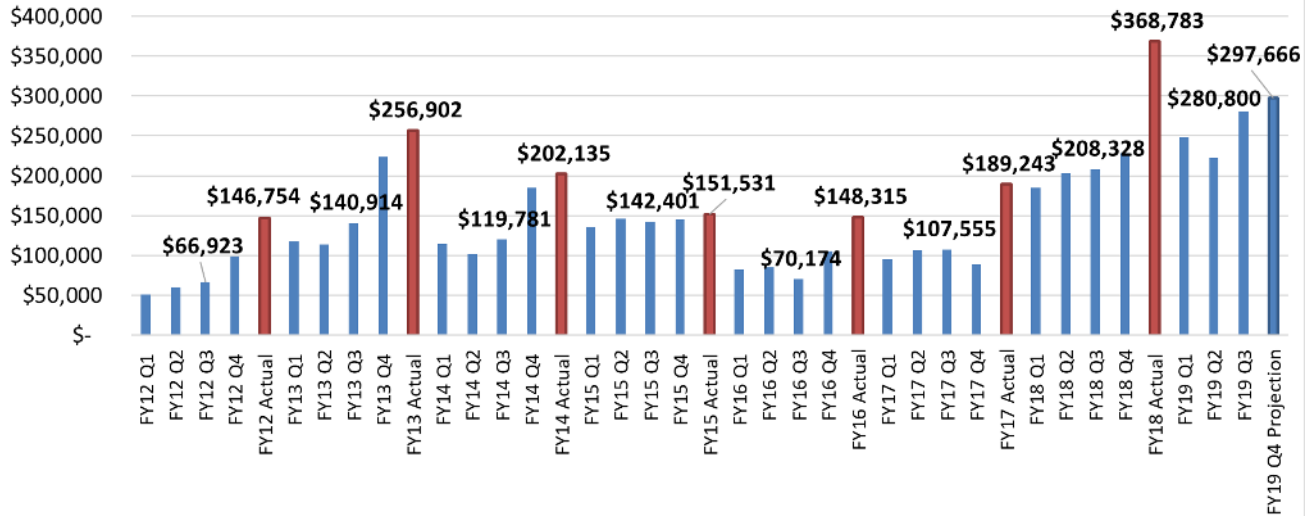
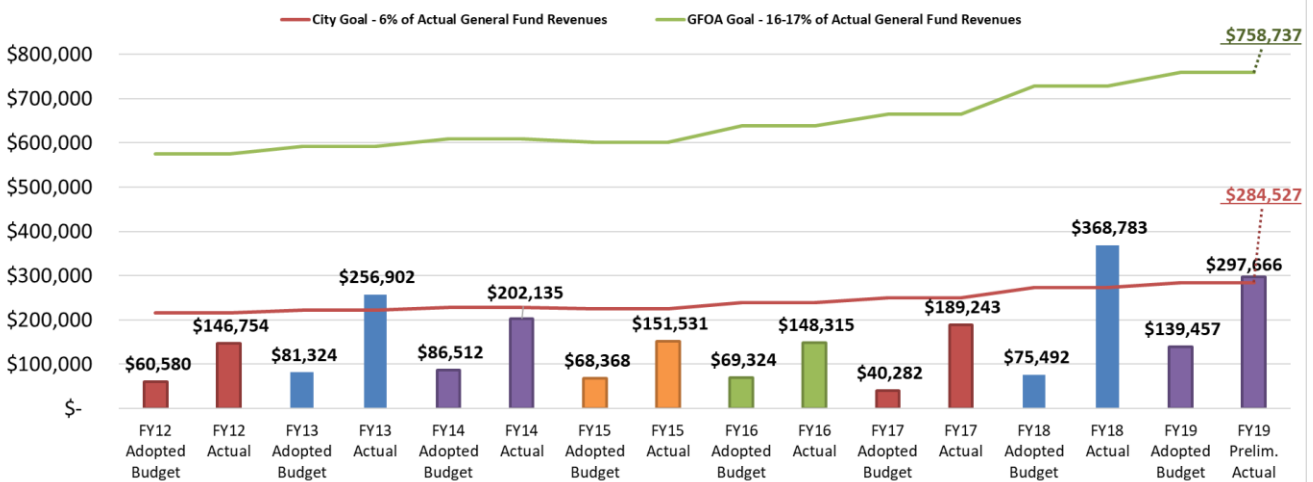*Chart 1: QCMR Projections (Blue) and Actual General Fund Balances (Red)[5]*

Chart 2: GFOA (16% of General Fund Revenues) and internal (6% of General Fund Revenues) goals compared to Actual fund balances

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[5] As highlighted in footnote 4, the budget includes contingency reserves and "Rainy Day Fund" deposits which are not reflected in the City's General Fund Balance. Over the course of the FY20-24 Five-Year Plan, the projected budget includes $140 million set aside for labor contracts, $286 million as a contingency againstcuts in federal funding, and $180 million in deposits to the Rainy Day Fund.
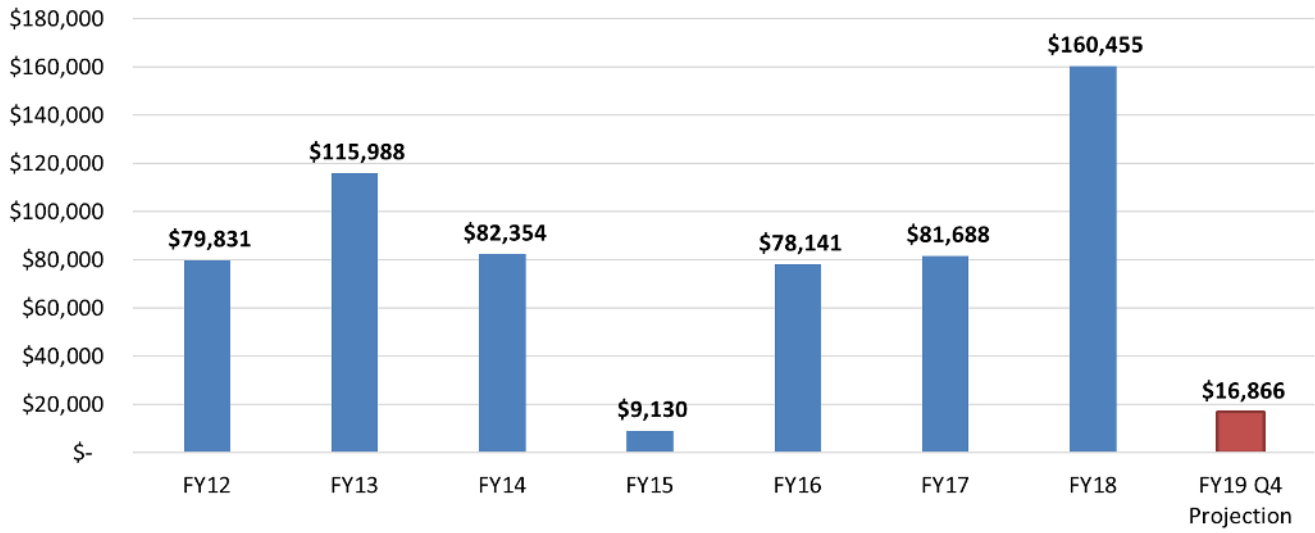
Chart 3: Difference between Q3 projection and Actual General Fund Balance figures
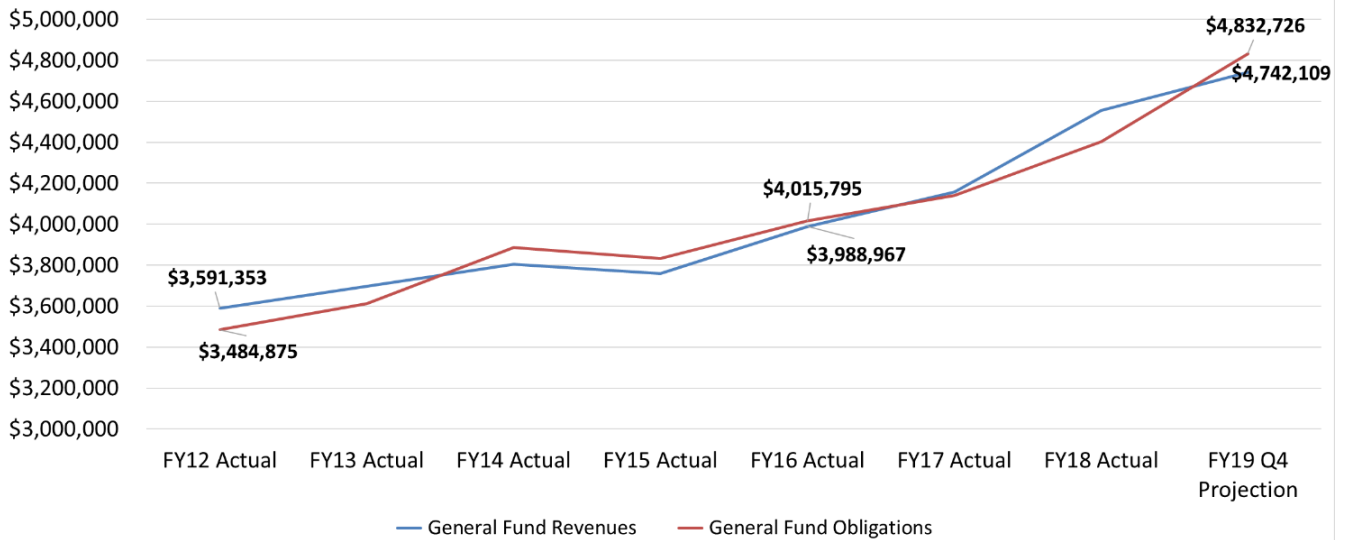

Chart 4: Highlighting the simultaneous growth of General Fund revenues and obligations

School District of Philadelphia Q4 Highlights

- **The School District of Philadelphia ended the fiscal year with a projected FY19 Year-End General Fund Balance of $214.4 million, $19.9 million above the Adopted Budget projection.**
    - Adopted Budget: $194.5 million
    - Preliminary Actual: $214.4 million
- *Local Tax revenues* ended the fiscal year with a projected **$10 million positive variance, above** original Adopted estimates.
    - Adopted Budget: $1.56 billion
    - Preliminary Actual: $1.57 billion
- *Operating expenditures* ended the fiscal year with a projected **$29.6 million positive variance, above** original Adopted estimates.
    - Adopted Budget: $3.13 billion
    - Preliminary Actual: $3.16 billion

According to the School District Q4 estimates, Local Tax and Non-Tax revenues ended the fiscal year relatively in-line with the the Adopted Budget. When the budget was adopted in June of 2018, the School District had projected $1.56 billion in Local Tax (e.g., Real Estate, Use and Occupancy, Liquor by the Drink, etc.) and Non-Tax revenues (e.g., City Grant appropriation, Philadelphia Parking Authority revenues), compared to the $1.57 billion actually collected (preliminary estimate), which represents a **$10 million increase in local revenues.**

Year-End expenditures also stayed largely in-line with Adopted figures. The $29.6 million increase in expenditures represents only a 1% increase over the Adopted Budget, if current year-end projections materialize. As shown in the graph below, this is mainly attributed to a $36.7 million increase in expenses for charter schools, **which was triggered by an increase in charter school tuition and unanticipated increases in cyber-charter enrollment.**
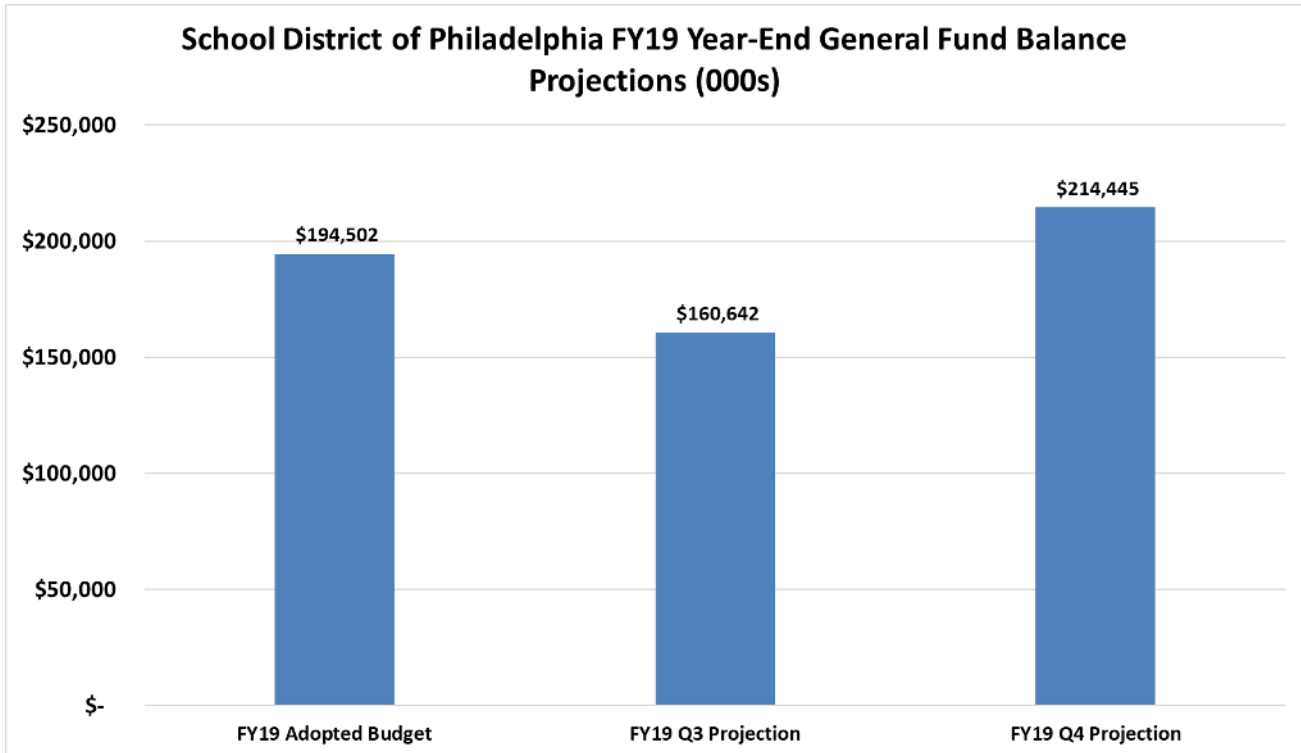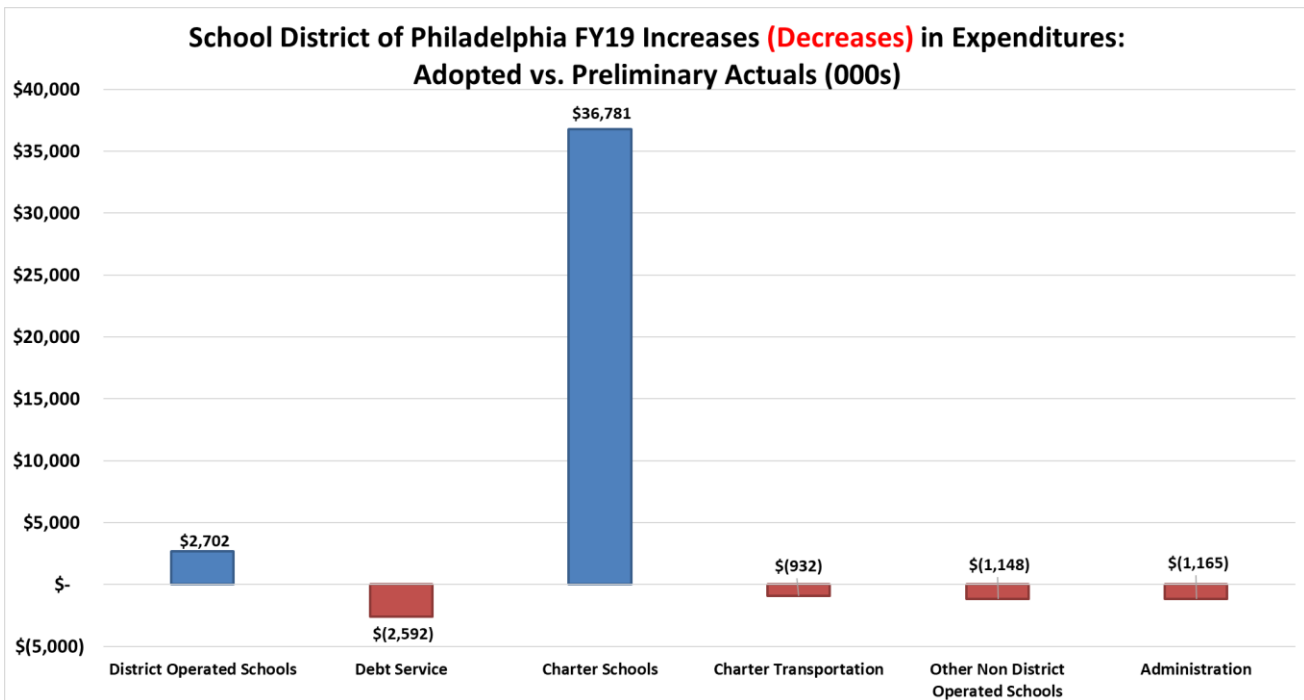
Chart 5: School District projections

Chart 6: How School District expenditures differed from projections

Pennsylvania Intergovernmental Cooperation Authority: July 2019 Revenue Update

On August 20th, the Pennsylvania Intergovernmental Cooperation Authority (PICA) released its first *Monthly Tax Revenue Update* for the new fiscal year (FY20), which compares year-to-date collections from FY19 and FY20 through the end of July. These updates allow us to track the ongoing trajectory of the City's revenues throughout the fiscal year.

When compared to *July of FY19*:

- *Wage and Net Profits* collections (City and PICA portion) are up 12.1% year-over-year.
- July *Beverage Tax* collections were 3.9% lower, when compared to July FY19. However, please bear in mind that the City has projected an annual 1% decline in tax revenues – due to decreased consumption of sweetened beverages.
- Overall, FY20 *Local Tax revenues* are 6% higher than at the same point last year, far outpacing the 2.4% Local Tax revenue growth projected in the City's FY20-24 Five-Year Plan.

Based on these preliminary figures, the City of Philadelphia began FY20 on a *positive* trajectory. However, month-to-month variation in revenues is to be expected and should not be solely relied upon to project future revenues. Throughout the fiscal year, City Council's *Finance and Budget Team* will continue to provide ongoing updates to members and staffers of City Council.